Internal Revenue Service

Department of the Treasury 200101037

Washington, DC 20224

UNIFORM ISSUE LIST: 401.00-00

Contact Person:

Telephone Number:

In Reference to:

Date: T:EP:RA:T:3

OCT 11 2000

Legend:

Company A =

Company B =

Company C =

Company D =

Company E =

Company F =

Company G =

Company H =

Plan X =

Plan Y =

Dear

This is in response to your letter dated September 24, 1999, in which you requested a ruling concerning the tax consequences of certain proposed distributions under section 401(k) of the Internal Revenue Code. Letters dated December 8. 1999, and June 9, 2000, supplemented the request.

On ************, Company A entered into an Agreement and Plan of Merger with Company B and Company C, a wholly-owned subsidiary of Company B, whereby Company

232

B would acquire all of the outstanding shares of common stock of Company A (the "Company A Acquisition"). At the time of the Company A Acquisition, Company A was, along with the following wholly owned subsidiaries: Companies E, F, G, and H, and other wholly owned subsidiaries, a traditional department store retailer operating approximately **** retail stores. Company A stores were located in 17 different states and operated under **** different store company names. Prior to the Company A Acquisition, Company A operated its business through its stores and warehouses, its corporate headquarters and its five regional headquarters located in the eastern, southern, southeastern, central and western parts of the United States. After the Company A Acquisition was finalized, Company A became a wholly-owned subsidiary of Company B.

A month later, Company A, Company B and Companies E, F, G, and H entered into an Agreement with Company D, an unrelated corporation, pursuant to which, upon the satisfaction of certain contingencies, including the execution of a definitive asset transfer agreement, and after the completion of the Company A Acquisition, Company B would transfer to Company D certain assets of Company A (the "Asset Transfer"). These assets did not comprise 85 percent of the assets of the former Company A and its wholly owned subsidiaries.

Under the terms of the Asset Transfer Agreement, Company D offered employment to all employees on the payroll at Company E stores and warehouses, except for 237 beauty salon employees, and to all employees on the payroll at the Company F, G and H stores, except for ***** beauty salon employees. Of the ****** employees of Companies E, F, G, and H offered employment, ***** accepted employment (the "transferred employees"). Of those ***** employees who became employed by Company D, approximately ***** had accounts in Plan X at the time of the Asset Transfer. As of *****************, approximately ***** had accounts in Plan X. The transferred employees continue to perform without interruption and in the same capacity, the same functions for Company D that they performed for Company A. Accordingly, Company B is no longer the recipient of the services of the transferred employees who were formerly employed by Company A and its wholly owned subsidiaries.

Prior to the Company A Acquisition, Company A sponsored and maintained Plan X. As of *****************, Plan X was merged with and into Plan Y, a profit sharing plan maintained by Company B which includes a cash or deferred arrangement as described in Section 401(k) of the Code and which is qualified under Section 401(a) of the Code. No distributions have been or will be made to Plan X participants on account of the merger of Plan X and Plan Y or on account of the Asset Transfer, unless such distributions are otherwise permissible under the terms of Plan X and the applicable Code provisions. Former employees of Companies E, F, G, and H who are now employed by Company D ceased active participation in Plan X on the date of the Asset Transfer and have never actively participated in Plan Y. Company D has never maintained Plan X, and no Plan X assets have been transferred to a plan maintained by Company D.

A number of transferred employees have requested distributions of their Plan X account balances. Company B proposes to offer these employees hired by Company D the opportunity to elect to receive distribution of their entire account balances now in the Plan Y, including account balances attributable to the 401(k) deferrals of such participants, provided that a favorable ruling is obtained from the Internal Revenue Service.

Based on the foregoing, you request the following rulings:

1) That the transferred employees of Company E, Company F, Company G, and Company H experienced a separation from service within the meaning of section 401(k)(2)(B)(i)(I) of the Code;

2) That the distribution from Plan Y of Plan X account balances attributable to the 401(k) deferrals with respect to participants who became employed by Company D pursuant to the offer of employment as described herein will not violate the distribution restrictions set forth in Section 401(k)(2)(B)(i) of the Code.

Section 401(k)(2)(B)(i) of the Code provides that amounts attributable to employer contributions made pursuant to an employee's election may not be distributable from a profit sharing plan earlier than (I) the employee's separation from service, death or disability; (II) an event described in section 401(k)(10); (III)the employee's attainment of age 59 ½; or (IV)the employee's hardship. Events described in section 401(k)(10)(A) include (i) the termination of the plan; (ii) the disposition by a corporation to another corporation of substantially all the assets used by the selling corporation in a trade or business; and (iii) the disposition of a corporation's interest in a subsidiary. Section 1.401(k)-1(d)(4)(iv) of the regulations provides that the sale of substantially all the assets used in a trade or business means the sale of at least 85 percent of the assets.

For tax years beginning prior to January 1, 2000, section 402(d) of the Code provided special forward averaging treatment for lump sum distributions from plans qualified under section 401(a). Section 402(d)(4)(A) provided that a lump sum distribution was a distribution or payment within one taxable year of the recipient of the balance to the credit of an employee which becomes payable to the recipient upon one of several events, including a "separation from service." Special forward averaging treatment of lump sum distributions was generally repealed by section 1401(a) and (c)(2) (subject to limited grandfather treatment) as part of the Small Business Job Protection Act of 1996, P.L. 104-188.

Rev. Rul. 79-336, 1979-2 C.B. 187, provides that, for purposes of the special forward averaging treatment of lump sum distributions under the earlier section 402(d) of the Code, an employee will be considered separated from service within the meaning of section 402(d)(4)(A) (formerly section 402(e)(4)(A)) only upon the employee's death, retirement, resignation, or discharge, and not when the employee continues on the same job for a different employer as a result of the liquidation, merger, or consolidation, etc. of the former employer.

As stated above, section 401(k)(10)(A)(ii) of the Code addresses the sale of substantially all the assets used in a trade or business. Rev. Rul. 2000-27 generally provides that, when an employer's sale of the assets of a trade or business does not constitute such a sale, distributions of elective deferrals from that employer's 401(k) plan may be made to the employees transferred as a result of the sale, but only if the change in their employment constitutes a separation from service within the meaning of section 401(k)(2)(B)(i)(I)

In this case, we have determined that Company A and its subsidiaries, Companies E, F, G, and H is a trade or business as defined in section 401(k)(10)(A)(iii) of the Code. As represented here, Company B sold to unrelated Company D less than 85 percent of the assets of this trade or business. Additionally, in the circumstances considered here, we have determined that the transferred employees are not employed in a continuation of the same trade or business. Under these facts, there has been a sufficient change in the employment status of the transferred employees to constitute a separation from service within the meaning of section 401(k)(2)(B)(i)(I).

Accordingly, we conclude with respect to ruling requests one and two, that the transferred employees experienced a separation from service within the meaning of section 401(k)(2)(B)(i)(I)) of the Code, and that the distribution from Plan Y of Plan X account balances attributable to the 401(k) deferrals with respect to the participants who became employed by Company D pursuant to the offer of employment as described herein will not violate the distribution restrictions set forth in Section 401(k)(2)(B)(i) of the Code.

The above rulings are based on the assumption that Plan X and Plan Y will be otherwise qualified under sections 401(a) and 401(k) of the Code, and the related trust will be tax exempt under section 501(a) at the time that the above transaction takes place.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that this ruling may not be used or cited by others as precedent.

A copy of this letter has been sent to your authorized representative in accordance with a power of attorney on file in this office.

Sincerely,

Frances V Sloan

Frances V. Sloan, Manager
Employee Plans Technical Branch 3
Tax Exempt and Government Entities Division

Enclosures:
Deleted copy of letter
Notice of Intention to Disclose

CC:

235